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INFO RUCNMER/MERCOSUR COLLECTIVE PRIORITY
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C O N F I D E N T I A L ASUNCION 000696

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PASS TO NSC DFISK, STATE FOR WHA/BSC MDRUCKER, BFRIEDMAN
AND MDASCHBACH

E.O. 12958: DECL: 10/08/2028
TAGS: [PREL](#) [ECON](#) [PGOV](#) [SNAR](#) [PA](#)
SUBJECT: SCENE-SETTER FOR BUSH-LUGO MEETING: PARAGUAY
CHARTS ITS OWN COURSE

REF: ASUNCION 665

Classified By: DCM Michael J. Fitzpatrick for reasons 1.4 (b) and (d).

SUMMARY

11. (C) President Fernando Lugo's administration represents the first break in Colorado Party's 61-year stranglehold on power; as such, it is shaking the foundations of Paraguayan society. President Bush's October 27 meeting with President Lugo offers the United States an opportunity to reaffirm its long-time friendship with Paraguay, convey strong support for the fledgling Lugo administration, build up a moderate democratic partner and counter Venezuelan President Chavez' influence in the Southern Cone. Lugo's challenges are many: An inexperienced team, exceedingly high expectations for change, endemic corruption, weak institutions, a divided Congress, and continued interference by Chavez. Lugo must generate jobs and promote economic development while downsizing the bloated state and tackling social and security issues - of key concern to his constituents. Lugo's top goals are fighting corruption and the underground economy, strengthening weak institutions and the rule of law, creation of a professional civil service, and economic growth/poverty reduction. Lugo continues to resist domestic and international pressures not to visit the United States at this time. Even efforts by the new GOP to reverse Paraguay's long-standing objections to U.S. positions in the WTO are now hampered by pro-Chavez elements here seeking to block closer ties with the U.S. If we are to continue to make in-roads with Lugo, we must make the most of his Washington visit, so that he returns to Paraguay convinced and able to demonstrate publicly that he can count on the United States. President Bush's interest in Paraguay, coupled with some firm offers of U.S. assistance, will go a long way with Lugo given his pragmatism and stated intention to steer his own "neutral" -- though democratic -- course. END SUMMARY.

LOCAL AND REGIONAL POLITICS

12. (C) Fernando Lugo's administration represents the first interruption in Colorado Party rule in 61 years, and as such, it is shaking the foundations of Paraguayan society. Former Catholic bishop Fernando Lugo won 40.8 percent of the vote in April national elections, 10.2 percent more than the Colorado Party presidential candidate. Lugo's Patriotic Alliance for Change (APC), a loose coalition of political parties, won a

large block of seats in Congress but does not have a majority. By voting overwhelmingly for change, the Paraguayan people gave Lugo a mandate for political, economic, and social reform. However, they also have high short-term expectations. Since his August 15 inauguration, Lugo has assembled a diverse team of politicians and technocrats to serve in his cabinet; he has encouraged each of his ministers to implement a 100-day plan to show the Paraguayan people that his government is making progress.

¶3. (C) President Bush's October 27 meeting with Lugo offers the United States an opportunity to reaffirm its long-time friendship with Paraguay, convey strong support for the fledgling Lugo administration, build up a moderate, democratic partner in the region, and blunt Venezuelan President Chavez' efforts to exert regional influence. Chavez, along with Bolivian President Evo Morales, is actively courting Lugo with his petro-dollars. When Chavez visited Paraguay for Lugo's inauguration, the two presidents signed 13 agreements, the texts of which have only recently been released and which bear little substance (septel).

¶4. (C) We believe Lugo is a leftist at heart, but a pragmatist of mind. He may already be growing tired of Chavez' aggressive and flamboyant style. Lugo has acknowledged the Washington-Caracas tug-of-war, and has said he is not Chavez, and will not blindly follow Chavez' Bolivarian plans. Lugo told Ambassador October 9 that international relations are between countries, not specific individuals, and are based on mutual respect and independence. (NOTE: Lugo specifically mentioned Chavez in this context, signaling that he is not enamored with Chavez

but values relations with Venezuela. He may have also been subtly telling his advisors that Paraguay's relations are not with the Bush administration but the United States. END NOTE). While Lugo appears resistant to some of Chavez' pressures, he is likely to be sensitive to attempts to strong-arm Paraguay or to undermine its independence or sovereignty, whether by Venezuela or the United States. Lugo appears to have played a helpful role in Unasur talks on Bolivia, and is developing constructive relationships with Uruguay, Chile and Colombia. He visited Washington for the first time in May 2007, and recently traveled to New York for the United National General Assembly. Lugo has traveled extensively since his April election.

AN UPHILL BATTLE

¶5. (C) Lugo's challenges are many: His inexperienced team needs to meet Paraguayans' high expectations for change, but will have to overcome endemic corruption, weak institutions, and a divided Congress to do so. He faces continued criticism related to President Chavez' attempts to interfere in domestic politics. Lugo does not have his own political party, and has distant (at best) relations with his Liberal Party vice president. His own inner circle continues to jockey for power and ideological influence. So far, Lugo has weathered the minor storms he has faced, but he has yet to develop a clear national agenda, or to engage in the political brokering which will be critical to his administration's success. A more in-depth discussion of some of Lugo's challenges follows.

THE ECONOMIC REALITY

¶6. (SBU) Lugo must promote economic development while cutting the size of the bloated Paraguayan state. Paraguay has inefficient state-owned monopolies in the rail, oil and gas, cement, steel, electricity, water, and telephone service industries. The economy is predominantly agricultural; agriculture represents about 21.9 percent of gross domestic product (GDP), and the economy is heavily dependent on exports of soybeans, cotton, grains, cattle, timber, sugar,

and electricity. Paraguay boasts vast hydroelectric resources, including the Itaipu hydroelectric dam built and operated jointly with Brazil, but fails to capitalize on those resources. The new government welcomes foreign investment, but widespread corruption and a weak judicial system are major deterrents to investment. Paraguay's real GDP in 2007 of USD 12.8 billion (in 2000 dollars) represented an increase of 30.6 percent from USD 9.8 billion in 2006. The underground economy, which is not included in the national accounts, probably equals the formal economy in size.

¶17. (SBU) U.S.-Paraguayan bilateral trade increased over the last six years, with the U.S. having a significant account surplus. U.S. imports from Paraguay were only USD 68 million in 2007; U.S. exports to Paraguay in 2007 were USD 1.2 billion. More than a dozen U.S. multinational firms have subsidiaries in Paraguay, and some 75 U.S. businesses have agents or representatives in Paraguay. As of March 2007, the total foreign direct investment in Paraguay stood at USD 1,602.52 million, and the United States was the largest foreign investor with USD 616.50 million. Paraguay and the United States annually discuss trade issues via the Joint Council on Trade and Investment (JCTI) such as U.S. certification of Paraguayan beef; technical assistance and investment in biofuels; FDA approval of Paraguay's natural sweetener stevia, and Paraguay's request for U.S. trade preferences. As the Commerce Minister likes to say, "we seeks trade, not aid."

PUBLIC SECURITY AND SOCIAL ISSUES

¶18. (SBU) Security and social issues are top concerns of Lugo's constituents. Violent crime is increasing in both urban and rural areas, and the public generally believes that Paraguayan security forces (particularly the notoriously corrupt police) do not meet their security needs. The

"landless" peasant movement has increasingly taken to protesting and "land invasions" -- illegally occupying large, privately-held ranches -- in agitating for agrarian reform. On some occasions, protests and "land invasions" have resulted in deaths or injuries.

¶19. (C) The Tri-Border Area (TBA) of Paraguay, Argentina and Brazil is a hub for trans-national criminal activity including drug trafficking, trafficking in persons (TIP), arms trafficking, intellectual piracy, and money laundering. Paraguay is a major transshipment point for cocaine from Colombia and Bolivia to Brazil, and Paraguay remains a major haven for money laundering. Paraguayan authorities often experience difficulties enforcing the law because of hostile geography, corruption, chronic understaffing, and the political and judicial power some drug traffickers wield. Paraguay took a giant step forward on money laundering, intellectual property violations, and trafficking in persons by passing a tougher penal code in June that will go into effect next year. Like his predecessors, Lugo is sensitive to "satanizing" the TBA, but has sent some promising signals by mentioning the need to eradicate terrorism during his speech at the United Nations General Assembly, and by signing agreements with Colombian President Uribe to promote collaboration in that area.

¶10. (SBU) Inefficient, state-run institutions dominate Paraguayan social services, and Lugo pledged to improve social services spending and make health care and education reform government priorities. Social services spending increased since 2003; however, most spending augmented employees' salaries. Many Paraguayans lack basic access to health care facilities, particularly in rural areas, and many more are uninsured. Government agencies and state-owned enterprises provide basic public services, but access is limited and services have deteriorated in quality.

LUGO'S GOALS AND U.S. ASSISTANCE TO PARAGUAY

¶11. (U) Lugo told the Ambassador in August his five-year goal was to leave behind strengthened democratic institutions better able to govern and resist corruption. In an October 8 IADB meeting, Lugo stated his goals as fighting corruption and informality, strengthening weak institutions and the rule of law, creation of a professional civil service, and economic growth/ poverty reduction. Reforming the National Police and land reform, including a national land survey, will be priorities. He has also promised improved social services and to promote a "social justice" agenda. Lugo and several key ministers told Ambassador October 9 that they are interested in discussing commercial issues (particularly beef and stevia), economic development and counternarcotics during Lugo's Washington visit. They promised to provide the Embassy with a draft agenda in coming days.

¶12. (U) U.S. assistance in Paraguay supports many of Lugo's goals, albeit at modest funding levels. USAID/Paraguay's FY08 budget is USD 7.8 million and focuses on Economic Growth; Improved Health Care; Sustainable Management of Natural Resources and Protected Areas; and Democratic Strengthening. USAID's Economic Growth Program ("Paraguay Vende") has generated over USD 60 million in additional sales and over 30,000 full-time job equivalents since 2003, thus supporting Lugo's goal to reduce poverty. Likewise, our Health Program supports Lugo's stated interest in improving basic health services. Specifically, it targets decentralizing health services, improving maternal and child care services, and increasing Paraguay's capacity to deliver family planning services. In the environment sector, USAID continues to support improved management of protected areas. Our Democracy Program focuses on fighting corruption, giving civil society a voice, and promoting decentralization and municipal development. Additionally, Paraguay's Millennium Challenge Account Threshold Program has provided USD 35 million over the past two years in an effort to fight corruption and formalize Paraguay's economy. Paraguay submitted its Stage Two Threshold proposal September 30, with great interest and support from Lugo and his economic cabinet. Post hopes the review process can be expedited so that President Bush can formally announce this assistance on or about October 27.

¶13. (U) The Embassy's Justice and Treasury Department advisors play critical roles in legal and financial reforms, including the new penal code, a new criminal procedures bill, customs enforcement, and budgetary and monetary policy. The Peace Corps has 180 volunteers -- its third largest mission worldwide -- serving throughout Paraguay. The Embassy's leading public diplomacy effort is its English language scholarship program, which identifies academically outstanding young Paraguayans from families with limited resources. Since the program's inception in 2006, the Embassy has awarded over 500 scholarships that enable Paraguayans to compete in the worldwide marketplace and qualify for other U.S. scholarship programs.

¶14. (C) USG support for the Paraguay Military Forces is second only to our support for Colombia in South America. U.S. Armed Forces provided the Military Forces' Joint Immediate Response Unit (DCEI) with more than USD 4.0 million in funding for weapons, equipment, and training in the past two years. The U.S. Armed Forces committed USD 4.1 million in Global Peace Operations Initiative (GPOI) funds and technical assistance to Paraguay's United Nations Global Peace Keeping Operations Program (UNPKO). In the absence of a formal Status of Forces Agreement (SOFA), U.S.-Paraguayan military cooperation continues, albeit scaled back and under a lower profile 505 Assurance Agreement signed in April 2007. Other security funding includes State's International Narcotics and Law Enforcement (INL) money, which along with DEA and U.S. Special Forces, assists Paraguay's Anti-Drug Secretariat (SENAD) in combating narcotics trafficking, money laundering, IPR violations, and trafficking in persons.

COMMENTS

¶15. (C) COMMENT: President Lugo continues to resist domestic and international pressures urging him not to visit the United States at this time. The president's chief of staff rebuffed Venezuelan attempts to convince Lugo to decline President Bush's invitation (reftel). Other ministers have recounted bitter internal battles to reverse Paraguay's three-year-old objections to the U.S. position at the WTO, as pro-Chavez elements (and Venezuela itself) seek to keep the objection in place -- if only to scuttle any closer commercial, trade, or political ties with the United States. In an October 9 discussion with the Ambassador about his U.S. visit, the former bishop "confessed" to the "almost original sin" of having been a bull-headed, anti-American leftist in his youth, a stance he now says he regrets. Lugo's commitment to meet with President Bush sends a strong signal regarding his desire for close relations with us - and to place a limit on Venezuelan interference.

¶16. (C) COMMENT (CONTINUED): If we are to continue to make in-roads with President Lugo, we must make the most of his Washington visit so that he can return convinced and able to demonstrate publicly that he can count on the United States. More so than any other president in modern Paraguayan history, Lugo has an opportunity to affect real change. However, the deck is stacked against him. We have an opportunity to forge a close relationship with Paraguay at a moment when there is growing anti-American sentiment in much of South America. Lugo's team has not yet articulated its goals for the presidential meeting itself, but is eager to work on an agenda. Lugo told Ambassador October 9 that the United States has a breadth of experience that Paraguay could learn from, in spite of the U.S.'s "own shadows." Lugo also expressed to the Ambassador great respect for "any U.S. president who wins re-election," and pointedly drew the distinction between U.S.-style democracy from the pseudo-democracy of autocrats like Chavez. President Bush's interest in Paraguay, coupled with some firm offers of U.S. assistance, will go a long way with Lugo given his pragmatism and stated intention to steer his own "neutral" -- though decidedly democratic -- course. END COMMENT.

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